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Reflections on the Theoretical Underpinnings of the General Purpose Financial Reports of Australian Government Departments

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Structured Abstract

Purpose - The purpose of this research is to determine the appropriateness of a general purpose financial reporting model derived from a ‘decision-useful’ framework for government departments.

Methodology/Approach - This research uses a survey methodology to access users of government department general purpose financial reports and is innovative because it has directly studied actual users across the entire public sector.

Findings - The findings of this research indicate that general purpose financial reports are used to satisfy financial accountability and public accountability rather than decision-making - indicative of users having an accountability focus rather than a ‘decision-useful’ focus. This provides systematic empirical evidence against the current financial reporting model used internationally in the public sector.

Research Implications - These findings have important implications for policy makers since the choice of an accounting framework has the capacity to affect the information content of reports – what is reported and how it is measured, and thus have a direct impact on the operations of government. The paper argues that it is crucial that public policy regulators re-examine the financial reports provided to stakeholders.

Originality – The research in this paper is original in that it has, for the first time, systematically reviewed all of the three elements of the public sector general purpose financial reporting model as well as directly accessing users. The authors can categorically argue for the abandonment of the model in favour of one which is better suited to the public sector.

Reflections on the Theoretical Underpinnings of the General Purpose Financial Reports of Australian Government Departments

ABSTRACT

Significant agendas of reform have been implemented in the Australian public sector including the adoption of accrual accounting. The public sector general purpose financial reporting model, like the private sector, is grounded in a 'decision-useful' framework. This model is premised on the existence of dependent users who are reliant on general purpose financial reports to make economic decisions. However, there have been doubts cast on the appropriateness of this premise for public sector organisations. This research determines the appropriateness of the model to government departments by empirically identifying users of government department general purpose financial reports and their information requirements. This research uses a survey methodology to directly access users of government department general purpose financial reports. The findings of this research are that general purpose financial reports are used to satisfy accountability needs rather than 'decision-useful' needs. These findings have important implications for policy makers since the choice of an accounting framework has the capacity to affect the information content of reports – what is reported and how it is measured, and thus have a direct impact on the operations of government.

KEY WORDS: Government Departments; General Purpose Financial Reports; Accountability; Decision Usefulness

INTRODUCTION

The last thirty years have seen significant reforms in the public sector. As part of these reforms public sector managers are now held accountable not only for the manner in which appropriated funds are dispersed, but also for the efficiency and effectiveness with which they use those funds (Guthrie, 1998; Chua and Sinclair, 1994; Ryan, 1998; Karan, 2003; Newberry, 2003). To satisfy these changed accountabilities the Commonwealth and State governments as well as local government authorities have adopted accrual accounting based on specific public sector accounting standards.¹

These public sector standards have been derived from the same ‘decision-useful’ conceptual framework used in the private sector. This framework which is operationalised through the Statements of Accounting Concepts (SAC’s) assumes that general purpose financial reports² will be useful for all public sector stakeholders.

However, the adoption of a ‘decision-useful’ framework for the public sector did not have universal support. A general purpose financial reporting model predicated on ‘decision-usefulness’ is essentially a market based model that assumes that the making of rational decisions, facilitated by the availability of appropriate information, will result in the efficient allocation of resources (Coy, Fischer and Gordon, 2001). The concern voiced, was whether a financial reporting model based on reporting profit could adequately explain the

performance of public sector entities, as well as discharging the entity's accountability obligations (Walker, 1989; Guthrie, 1998; Ma and Mathews, 1993; Stanton and Stanton, 1998; Conn, 1996). Specifically it has been argued that differences in the roles and operating environments which have the capacity to effect the type of information needed to assess the performance of the public sector and discharge accountability were ignored (Barton, 2005).

This research, through an empirical interrogation of each of the elements of the general purpose financial reporting model will address the fundamental applicability of the 'decision-useful' framework to the public sector. The paper proceeds as follows. The next section will address the theoretical perspectives of public sector accounting. This will be followed by a review of previous empirical studies which have addressed the individual elements of the general purpose financial reporting model. The remaining three sections will describe the research method employed, report the results of the research and discuss the findings and the implications of the research.

THEORETICAL PERSPECTIVES OF PUBLIC SECTOR REPORTING

The formal accountability relationship in both the public and private sectors is one of principal and agent (or superior and subordinate), where agents are held accountable to, and receive direction from, their principals (Mulgan, 2000). Mayston (1993) has argued that principal/agent theory is a lens through which

accountability can be viewed. In this vein, Broadbent and Laughlin (2003) address the problems posed by the principal/agent relationships and how they may be resolved. They identify two different streams in the principal/agent literature. While both streams acknowledge the assumption that agents are self-seeking and that mechanisms must be devised to ensure that agents act in the best interests of the principals, they differ in the manner by which they propose to accomplish this. The first stream of literature, which could be described as a contractual response, has concentrated on designing and refining contracts to align the interests of agents with principals and therefore control their actions. This response to the agency problem is most suited to those situations where the accountability relationship is well defined and easier to control. Much of the accountability literature in the private sector, where the accountability relationships are less complex and consequently easier to control, is placed in this first stream.

The second stream recognizes that accountability relationships between principals and agents that are complex and open-ended or not explicitly defined are not easily monitored by contracts. Consequently, this stream has concentrated on the use of different forms of accountability mechanisms as a means of ensuring the behavioural compliance of the agent. This literature recognises that the level of control that can be exercised by principals over agents may differ. This is particularly the case in the public sector. Broadbent and Laughlin (2003) note that a particular feature of public accountability is that governments are accountable for *authority* that has been granted to them rather

than for *responsibility* that has been granted to them as is the case in the private sector. Consequently, public accountability is more open-ended and less able to be controlled (Day and Klein, 1987).

These differences in accountability relationships have important implications for the choice of a framework to underpin the preparation of general purpose financial reports. The contractual response to the principal/agent problem is more aligned with the private sector ‘decision-useful’ framework. The adoption of this ‘decision-useful’ framework in the public sector implies that the principal/agent problem in the public sector is also able to be satisfied by this contractual response. However, the ability of the ‘decision-useful’ framework to discharge public accountability has been questioned by several researchers. Both Pallot (2003) and Funnell (2003) identify the concerns of Auditors – General (in New Zealand and Australia respectively) that the adoption of private sector ‘decision-useful’ reporting models is inconsistent with the discharge of public accountability. Similarly Karan (2003) has noted that the introduction of private sector accounting standards into the public sector has seen a diminution in public accountability.

Advancing this argument one step further, and perhaps as an explanation for it several commentators have noted that the information disclosed under an accountability framework will differ from that disclosed from a ‘decision-useful’ framework. Ijiri (1983) contends that the adoption of either an accountability framework or a decision-usefulness framework will critically affect the financial

reporting model. The models that result from the adoption of either framework result in differences in the information provided. Ijiri's contentions are supported by the prior research of Gjesdal (1981) who, in an empirical analysis, determined that the criteria of stewardship informativeness and decision-making informativeness were not identical and that as a consequence there is reason to differentiate between the two. The effects of this differentiation can be seen in later literature, where it has been argued that the 'decision-useful' framework for general purpose financial reporting, limited as it is to the provision of information for making economic decisions, can not provide information about issues such as fairness, equity and accessibility (Williams, 1987; Parker and Gould, 1999; Coy, Fischer and Gordon, 2001). Pallot (1991) argues that accountability models based on rights and contracts are incomplete in that they do not take account of issues such as need and equity. These issues are central to the operations of the public sector.

The debates about an appropriate accounting framework are not merely theoretical arguments (Hopwood, 1984). They have profound implications for the conduct of the sector. Many have argued that the introduction of the private sector based framework has meant that aspects of the operations of the public sector that were not previously reduced to financial presentation are now being reported in that manner, and this, in turn, has the potential to affect not only the way the public sector is viewed and assessed, but also the way in which it carries out its functions (Hopwood, 1985; Revsine, 1991; Gray and Jenkins, 1985; McCrae and Aiken, 1994; Aiken, 1994 and Aiken and Capitano, 1995). Others

have argued that the information provided and reported by accounting systems can create its own reality (Hopwood, 1984; Wilmott, 1985; Hines, 1988; Guthrie, 1998; Boyce, 2000). Further, these researchers contend that, accounting systems have the capacity to influence the direction that organizations and entities will take in the future because of the emphasis placed on particular information and the aspects of an organization that the accounting system has made visible.

In addition to these more theoretically derived arguments, other concerns were expressed that the ‘decision-useful’ framework was adopted with little empirical or analytical evidence as to who were the users of public sector general purpose financial reports, what their information requirements were and the purposes for which they required information (Walker, 1989). Rutherford (1992) argues that the paucity of empirical evidence as to the identity of users of financial statements in the public sector and their decisions makes the ‘decision-useful’ framework for general purpose financial reporting in the public sector difficult to justify.

Several researchers have attempted to address these empirical issues as part of the continuing debate about the applicability of a ‘decision-useful’ framework for general purpose financial reporting in the public sector. The next section describes the general purpose financial reporting model as it is currently prescribed and reviews the prior literature which has attempted to identify the users of public sector general purpose financial reports and their information needs.

INSIGHTS FROM LITERATURE

‘Decision-useful’ framework of the general purpose financial reporting model

The three elements of the model are identified and described in Statement of Accounting Concept 2 *Objectives of General Purpose Financial Reporting* (SAC2). First it identifies the *users* of general purpose financial reports. It then identifies why users may require information before prescribing what information users will require.

In relation to the first element – users – the move to international accounting standards for reporting periods ending on or after 1 January 2005, means that the Australian Accounting Standards Board is replacing existing standards and concept statements in line with those of the International Accounting Standards Board. *Statements of Accounting Concepts 1 and 2* remain and the *Framework for the Preparation and Presentation of Financial Statements* comes into force. The relevance of this for this paper occurs in relation to the classification of users. SAC 1 and 2 refer to dependent (those who must rely on general purpose financial reports to obtain information) and non-dependent users, while the Framework refers to internal and external users. While there is considerable convergence between the two classification systems it should be noted that the classification of non-dependent users can include external users who are able to command the provision of information specific to their own needs as well as internal users who by virtue of their role within an entity have alternate or

supplementary information sources (management accounting reports for example). In addition, the extant literature (see for example Coy et al., 1997) commonly refers to the external/internal split. For the purposes of this research external and internal are used.

In relation to the second element, what information is required, SAC 2 determines that in order to meet the information needs of users, general purpose financial reports should provide information about the performance of the entity, the financial position of the entity, the financing and investing activity of the entity and compliance matters. With regard to the third element of the model - the purposes for which information is required, SAC 2 takes the position that in view of the information needs of the users identified in the statement, the objective of general purpose financial reporting is 'to provide information to users that is useful for making and evaluating decisions about the allocation of scarce resources' (para 26). Further, it is asserted that when general purpose financial reports meet this objective they will also enable entities to discharge their accountability obligations. In short, SAC 2 prescribes a financial reporting model that has three elements, *external users* requiring *general purpose financial information* for the purposes of *making decisions*

Research that has investigated the individual elements of the model

The prior approaches to identifying *users and their information needs*, can be broken into three groups reflecting three different methodologies. First, there are

those studies that have used normative arguments to identify user groups or classifications. The seminal work in this area is that by Anthony (1978). Anthony argued that in order to be useful, any list of user groups must be brief. His study normatively identified five categories of user; governing bodies, investors and creditors, resource providers, oversight bodies, and constituents. Other normative researchers have also determined user lists with varying amounts of commonality in identifying user classifications (see for example Holder, 1980; Office of the Auditor General of Canada and the United States General Accounting Office, 1985; Jones et al., 1985; Drebin, Chan and Ferguson, 1981).

Second, there are those empirical studies which have used these normatively identified classifications of users to either further investigate the identification and composition of user groups or their associated information needs. Using this approach, these studies have identified additional *users groups (the 'who' question)* which had not been normatively determined. Atamian and Ganguli (1991) found that other municipalities were common recipients of the financial reports of municipalities in the US. Internal management was identified as users of financial information by both a US study (Van Daniker and Kwiatowski, 1986) and a Spanish study (Alijarde, 1997).

Other empirical studies sought to determine what information is needed by users. Three studies have examined this in the context of government departments; Jones et al., (1985), Hay and Antonio, (1990) Crain and Bean, (1998). All

identified that user groups were interested in performance information and in the cost of services provided rather than general purpose financial information. These results have been replicated in UK and Australian studies for both government departments and local government authorities (see for example Robbins, 1984; Jones et al., 1985; Daniels and Daniels, 1991; Collins Keenan and Lapsley, 1991 and Priest, Ng and Dolley, 1999).

There has been limited investigation of the purposes for which users require information (*the 'why' question*). In a US study Jones et al., (1985) sought information on the purposes for which government and municipal users required information and the types of decisions made. The results of the survey indicated that accountability and decision-making were both important reasons for which users required financial information. Two Australian studies, Jones and Puglisi (1997) and Mignot and Dolley (2000) investigated the usefulness of general purpose financial reports for making decisions.

The first study surveyed preparers of government department financial reports and found a lack of support for the introduction of accrual accounting techniques and also for the decision usefulness of reports prepared on an accrual basis. The second study also conducted in a government department context, investigated whether two groups of previously identified users, legislators and interest group members, found financial statement information useful in a decision-making task. The results of this research support the 'decision-useful' framework for

general purpose financial reports insofar as they indicate that both user groups found general purpose financial reports useful for decision-making.

A third group of studies has taken an entirely different approach to the previous two groups in that they have sought to empirically identify actual users and their information needs within the context of specific public sector entities. Of particular relevance are Coy et al., (1997) and Clark (2002) which both used the approach of surveying the actual users of specific reports in their attempts to obtain information about users and their information needs. Coy et al., (1997) sought to identify the users of tertiary education institutions' annual reports and their views on the qualities and disclosures in the annual reports which they received. They placed cards requesting recipients to participate in the research in all copies of the annual reports distributed by New Zealand tertiary institutions. Those recipients who returned the cards were then surveyed.

The study revealed that of the recipients who identified themselves by returning the cards, 60% had a role in the management, operation or governance of the institutions, 10% were involved in other educational institutions' management (other like entities), 25% were managers of businesses or employee organisations and the remainder were journalists, librarians, Members of Parliament and members of the general public. The findings of this study that internal users were more predominant than external users are inconsistent with most of the theoretical studies previously discussed that emphasise external users.

Clark (2002) investigated the recipients of departmental annual reports in Victoria, Australia – in particular who used those reports and the purpose for which they were used. He did not examine what information was used. Consequently, the results of this study need to be interpreted in the context that the study did not seek to separate the use of the annual report in general from the use of general purpose financial reports in particular. However, this study confirms the findings of the Coy et al., (1997) study that internal management and ‘other like entities’³ were significant user categories. The study also confirmed the existence of the broad user groups identified by the conceptual framework in the context of government departments. In addition, the results indicated that nearly one third of all respondents found annual reports useful for reasons other than those specified by the conceptual framework. Clark concludes that the application of the ‘decision-useful’ framework to both the private and public sectors may have failed to adequately capture the purposes for which users find the annual reports of government departments useful.

In summary, the review of the literature indicates that the majority of studies have made a contribution to obtaining an understanding of primarily one element of the general purpose financial reporting model. There remains a gap in the literature in terms of a **systematic understanding of the three elements of the model** for a specific public sector entity type. This research will fill this gap and as a consequence enable an assessment to be made of the applicability of a private sector general purpose financial reporting model derived from a

‘decision-useful’ framework to the more complex accountability environment of a public sector government department.

RESEARCH METHODOLOGY

Research Approach

The objective of this study is to empirically investigate the identity of users of public sector general purpose financial reports and their information needs. To do this, a survey approach has been adopted. Government departments were chosen as the specific entity to be investigated. The general purpose financial reports of government departments are primarily distributed as part of the annual report. Therefore, in order to determine the identity of users of general purpose financial reports for government departments, this research surveyed the recipients of the 1998/1999 annual reports of government departments. This time frame was selected for two reasons. First, it was the annual report that was most current at the time the research was being conducted. Second, it was noted during discussions with the relevant government departments that there were increasing pressures to publish annual reports on the internet rather than distribute them directly to recipients. However, at the time the research was conducted, it was not common practice. Consequently, there was a ‘window of opportunity’ in which to gather information about users of annual reports. Once annual reports were freely and widely available on line, the question of determining and directly accessing annual report users becomes more complex.

Sample Selection

Queensland was chosen as the site of the study⁴. In terms of selecting departments for inclusion in the study the sampling strategy was aimed at obtaining access to a wide range of users.

Government departments have been classified as either central agencies or line departments (Nichols, 1991; Funnell and Cooper, 1998; Fitzgerald et al., 1996). Central agencies are generally described as those departments which have the responsibility to provide advice and support to the executive government on such issues as whole of government co-ordination and future directions. Line departments are also referred to as service departments reflecting their service delivery role (Wanna, O'Faircheallaigh and Weller, 1992). This distinction is important for the purposes of this study because it is likely that the identity of users and the information needs of those users will vary between central agencies and line departments. Therefore, departmental entities from each of these categories were chosen for inclusion in this study.

A complete list of Queensland government departments existing at the time of the study is contained in Appendix B. In Queensland, there were three central agencies at the time of the study; the Department of Premier and Cabinet, Queensland Treasury, and the Department of State Development (Fitzgerald et al., 1996). For the purposes of this study, Queensland Treasury was chosen as an example of a central agency, as it was the largest of the central agencies.

In relation to line departments, the largest spending departments in Queensland are the Departments of Health and Education. The Department of Health was included in the study. However, the Department of Education was excluded from the study because of differences in the way it distributed its annual report compared to other departments.⁵ The second line department included in the study was the Public Works Department. The Public Works Department is an example of a smaller department and as well operates Commercial Business Units. It was anticipated that there would be a broader spectrum of users in this department, compared to a line department that has no commercial activities. Two further line departments – Department of Corrective Services and Department of Aboriginal and Torres Strait Islander Policy – were also selected for inclusion in the study. These two departments were selected as it was felt that they might have different users with different information needs because of the ‘sensitive’ nature of their undertakings and the fact they are likely to be the subject of media attention. In summary the five departments which were chosen for inclusion in the study were - Queensland Treasury, Queensland Health, Department of Public Works, Department of Corrective Services and Department of Aboriginal and Torres Strait Islander Policy.

Research Instrument

Recipients received a research instrument specific to the entity for which they received an annual report. Questions one to four, sought to determine who used the annual reports; questions five to eight, elicited information about what

information was used by the respondents; and question nine asked respondents why they wanted the information contained in general purpose financial reports.

Who Uses Annual Reports?

In order to identify accurate user groups, respondents were asked to self-assess the nature of their relationship with the entity. The 7 categories used in this analysis; (ratepayers/taxpayers, other resource providers, elected officials, other recipients of services, oversight bodies, internal management and other like entities) are those that have been commonly agreed in both the normative and empirical public sector accounting literature (see for example Anthony, 1978; CICA, 1985; SAC 2, 1990; Coy et al., 1997; Clark, 2002). In the analysis which follows, the users are broken into external users (ratepayers/taxpayers, other resource providers, other recipients of services, oversight bodies and other like entities) and internal users (elected officials ⁶ and internal management).

What information is used?

Obtaining data about the information needs of users highlighted some of the problems inherent in mail survey research. This research sought to identify information which respondents actually use in the annual report, and in particular whether they used the general purpose financial reports contained within the annual report. Leftwich (1980) has identified that in a costless environment users will require more information than they actually use. In survey research, where the researcher is not present when the survey is being completed, there can be a

problem in ensuring that respondents fully understand what is being asked of them (Emory and Cooper, 1991; Stone, 1978).

The issue of how to differentiate between information that users might want to be disclosed, but may not necessarily use, and information that they do actually put to some purpose was resolved by asking questions which enabled participants to address both issues directly. In one question respondents were asked to identify on a five point Likert scale *the importance* of disclosing certain items of information in the annual report. The list of items that was included was drawn from the format of annual reports themselves, from the professional pronouncements, and the prior literature. This question allowed respondents to indicate in general terms, information they thought should be disclosed even if they did not actually use it. It was effectively used as a screening device but not used in analysis. The information used in analysis was obtained from a second question designed to determine what information in the annual report respondents used. Respondents were asked to indicate, once again on a five point Likert scale, *the emphasis* that they placed on information disclosed in the annual report when they were reading it. This question, while it encompassed the items in the first question utilised common annual report headings so that it more specifically related to the information respondents actually received.

Why is information used?

To determine the purposes for which users require information, respondents were asked to indicate on a five point Likert scale how useful the information

contained in the financial statements was in making a wide range of decisions and satisfying a number of accountabilities. These decisions and accountabilities were drawn from SAC 2, Australian Accounting Research Foundation (AARF) sponsored discussion papers and prior literature. They range from very broad decisions such as 'to decide how to vote' to very specific ones such as 'to inform a decision as a supplier of goods, services or finance'. Examples of the accountability requirements of users included 'to determine if the organisation has operated in the best interests of the community' and 'to determine the effect of current operations on future generations'.⁷ Responses to this question allowed an understanding of the purposes for which users used general purpose financial reports. Respondents had the opportunity to indicate whether there were any further uses, other than those already identified, that they had for financial report information.

RESULTS AND ANALYSIS

In all, 1,262 research instruments were distributed and 289 useable responses were received giving a response rate of 22.9%. This response rate compares favourably with response rates achieved by other surveys of this type (Jones et al., 1985 – 10%; Priest, Ng and Dolley, 1999 – 19%, Coy et al., 1997 – 56%).⁸

Who uses information?

Table I shows for each user category the number of respondents who identified themselves as belonging to that category. Three observations can be made from an examination of this table.

Take in Table I

First, all of the user categories identified by SAC 2 were empirically identified. Second, the user group ‘other like entities’ (in this case other government departments) identified by prior studies but not by SAC 2 have been identified in this research. This group comprises 20% of all respondents. The identification of ‘other like entities’ as a significant user category in this research is consistent with prior empirical research. Atamian and Ganguli (1991) found ‘other municipalities’ (other like entities) were a significant category of user in a local government context. Coy et al., (1997) also identified other tertiary institutions as recipients of the annual reports of New Zealand tertiary institutions. Clark (2002) confirmed the findings of both Coy et al., (1997) and Atamian and Ganguli (1991) in a government department context when he argued that ‘the most common category of users were those in sister or competitor organizations’.

A third observation is that 35% of users identified are internal users, that is, users who are not dependent on general purpose financial information to meet their information needs. The identification of ‘internal management’ as a user group (nearly 30% of users) confirmed the findings of prior normative and empirical

research that this group is a significant user group (Davidson, 1977; Jones et al., 1985; Atamian and Ganguli, 1991; Coy et al., 1997 and Clark, 2002).

These findings, even on the first element of the model – users - begin to cast doubt on the model’s veracity to the extent that the specification of the general purpose financial reporting model clearly excludes a large percentage of users.

What information is used?

To determine what information in the annual report was used, respondents were asked to indicate on a Likert scale of one to five (where one was ‘no emphasis’ and five was ‘strong emphasis’) how much emphasis they placed on 13 disclosure items contained in the annual report they received.⁹ Factor analysis was performed on the responses by participants to ascertain whether the disclosure items could be reduced to a smaller number of variables that reflected common themes.¹⁰ As a result of the factor analysis, three factors were identified. The factors are shown in Table II.

Take in Table II

Each of these factors reflects identifiably different information types or themes. The first factor includes the individual elements of the general purpose financial reports required to be produced by government departments and is named *general purpose financial reports*. The second factor comprises information items that have both numeric and narrative elements and which, when taken together, provide an overview of a department’s performance beyond (but including) financial performance. It is named *performance information*. The

third factor comprises information items that are narrative in nature and has been named *narrative information*. Factor scores were calculated for each respondent.¹¹

Table III reports the mean factor scores for all users and for external and internal users.¹² The results reported in Table III indicate that *performance information* is the information factor on which most emphasis is placed by all users. However the results also indicate that both categories of users place some emphasis on general purpose financial reports.¹³

Take in Table III

Again, in relation to the second element of the model, the findings indicate that one of the key pieces of information that users require is performance information, and the general purpose financial reporting model only caters in part to this, by including some subset of this information – financial information.

Why information is used?

In determining the use made of general purpose financial reports, respondents were asked to indicate, on a Likert scale of one to five (where one was ‘not useful’ and five was ‘very useful’), how useful information contained in the general purpose financial reports was in making judgements or decisions. The research instrument presented a wide range of alternative decisions and judgements to respondents. These were drawn from a variety of sources including SAC 2, AARF sponsored discussion papers and prior literature.

Factor analysis was again used to simplify the data and identify a smaller number of variables which reflected common themes. The factors that emerged as a result of the factor analysis and the variables of which they are composed are shown in Table IV.

Take in Table IV

The elements of the first factor can be characterised as having a basis in the financial operations and financial performance of the entity including comparisons with other organizations. This first factor was titled '*financial accountability*'. The second factor which was titled '*public accountability*' included decisions/judgements that relate to overall or general accountability for the operations of the entity. The third factor included decisions that users may make as a result of the information presented in the financial statements and is related to the 'decision-usefulness' concept. It was titled '*decision-making*'. Again, factor scores were calculated for each respondent.

Table V reports the mean scores for all users, external users and internal users for each of the identified factors.

Take in Table V

Inspection of the results reported in Table V indicates that all users, find financial statement information most useful for the purpose of '*public accountability*'. In addition, they regard financial statement information as being more useful for discharging *financial accountability* and *public accountability*

than for *decision-making*. They do not find financial statement information to be useful for ‘decision-making’.

Again, in relation to the third element of the model, the findings indicate that users are using information supplied for the purposes of public accountability, not decision-making. This seems to point again to a preference for an accountability framework rather than a decision-usefulness framework.

In sum, this research supports prior empirical research in identifying major user categories not identified by accounting regulators (see for example Van Daniker and Kwiatowski, 1986; Coy et al., 1997; Clark, 2002). Further, while the results of this research indicate that use is made of the general purpose financial reports of government departments they indicate that these reports are not used for the purpose of decision-making, the key premise of the ‘decision-usefulness’ framework. Rather, general purpose financial reports for government departments are most useful for satisfying accountability needs and that performance information is needed to assist in discharging these needs.

FINDINGS AND IMPLICATIONS OF THE RESEARCH

The major finding of this research concerns the purposes for which information is required, and the implications this has for the basis from which general purpose financial reports are prepared. The finding that general purpose financial reports are used to satisfy accountability requirements rather than for economic

decision-making is indicative of users having an accountability focus rather than a 'decision-useful' focus. Ideally, reports prepared from an accountability framework would contain different information than those prepared from a 'decision-useful' framework (Williams, 1987; Parker and Gould, 1999; Coy, Fischer and Gordon, 2001). The provision of information concerning profit and loss and financial position is not so critical in government departments devoid of a profit motive. What is important is the provision of information that will allow an assessment of the effectiveness of the department in meeting its objectives (Barton, 2005).

The findings of this research support prior work which has addressed specific issues associated with the adoption of a 'decision-useful' framework (see for example Carnegie and Wolnizer, 1995; Carnegie and West, 2003; Pallot, 1999; Carlin, 2000; Ma and Mathews, 1993; McCrae and Aiken, 1994). Specifically they provide empirical support for the contention that private sector based accounting concepts and standards do not provide information that is relevant to assessing the performance of government departments (Walker, 1989; Barton, 2005).

Moreover the findings for the information content of the general purpose financial reports of government departments support the contention that the current general purpose financial reporting framework is not relevant for users needs. Users in this research indicated that they preferred performance information to general purpose financial information. These results are consistent

with the assessments of a growing number of researchers (Walker, 2002; Carlin and Guthrie, 2001; Sharp and Carpenter, 1998; Rutherford, 1992) that the information contained within general purpose financial reports as they are currently constructed is insufficient to satisfy the needs of users in the public sector and that performance information is also required.¹⁴ Moreover, they provide support to the calls for the adoption of a service efforts and accomplishment (SEA) reporting regime such as that which exists in the USA in the Australian public sector (Walker, 2001; Pallot, 2001). The SEAs reporting regime classifies performance indicators and provides accompanying contextual data and interpretive commentary on results. The focus of service efforts and accomplishments reporting is to improve the quantity of information available to both government and the community about the performance of government services, and to present it in a form that is readily understood.

Indeed regulators in a number of Australian jurisdictions appear to be acknowledging the deficiencies of the general purpose financial reporting model in terms of the information supplied and are making moves at the margins to remedy this. For example, in Western Australia and Victoria, government departments include performance information in their annual reports. In Queensland the Public Accounts Committee (2001) has recommended that ministers encourage agencies to disclose performance information as part of their annual report. Further, Queensland local government authorities have been required, since the end of the 2003 financial year, to produce community financial reports in an attempt to make local government annual reports more

‘user friendly’ (Cunningham, 2001). The community financial report must be consistent with the audited general purpose financial reports but must present information about the financial performance and position of the authority in a manner that can be readily understood by the community. Further, it must provide a commentary on the meaning of the financial results. It would appear to be imperative that public policy regulators, as a matter of urgency, review financial reporting mechanisms to ensure that they provide meaningful information about the performance of the public sector within the context of the espoused objectives of public sector organisations.

More significantly, because the data for this research was obtained on **all three elements of the model**, broader, and more penetrating implications can be drawn from this research. The findings support the suggestion by several authors (see for example, Coy, Fischer and Gordon, 2001; Barton, 1999; Pallot, 1999) that an alternate framework for reporting in the public sector should be further developed. Ijiri (1983) and others have noted that the information that is provided under an accountability framework will be different to that which is provided in a ‘decision-useful’ framework. This research has confirmed that it is unlikely that the more complex and open-ended accountability relationships between principals and agents can be monitored by the contracts implicit in the private sector oriented, narrowly focussed ‘decision-useful’ framework.

The accounting and reporting framework adopted by an organization or group of organizations is not a trivial matter. The choice of an accounting and reporting

framework has social and public policy implications for public sector entities including government owned corporations (Ijiri, 1983; Hopwood, 1984; Revsine, 1991; Gray and Jenkins, 1993; McCrae and Aiken, 1994; Aiken, 1994; Aiken and Capitanio, 1995). Hopwood (1984, p.170) argues in reference to accounting that 'as a means of collecting and reporting selective patterns of information it has played a not insignificant role in the construction of public organizations and policies'. Accounting from this perspective is a construct that plays an active role in the management of public sector organizations. In particular, Aiken and Capitanio (1995) claim that the adoption of accrual accounting techniques in the public sector have contributed to a lack of goal congruence and financial control amongst the entities that comprise the public sector. As a consequence macro-economic planning and control as they have been practised are compromised as the public sector, at least at an unofficial level, becomes fragmented. As a tangible example of the adoption of a particular reporting framework they warn that the subjectivity introduced by accrual accounting techniques has placed parliamentary conventions which enable scrutiny of the executive, particularly with regard to the appropriate use of public funds, at risk.

There are two limitations of this research. The first limitation lies in its reliance on the use of a mailed survey as the data collection method. Survey data cannot be considered factual but rather the perceptions of fact by the respondents. Further, there is no guarantee that the person to whom the research instrument was sent is the person who actually completed the survey. In addition, the use of a mailed survey leaves open the possibility that the respondents did not

understand the questions properly and this could affect their answers. The second limitation to this research concerns the manner in which users of general purpose financial reports have been identified in this research. Users who have accessed the annual report by borrowing it from a library, another user, or obtaining it from the internet have not been identified. Although it is argued that at the time of this research these users would only represent a small number of users, it remains a limiting factor to the research.

The findings of this study provide a rich foundation for future research. There are two main avenues for future research. First, the findings of this research that users of the general purpose financial reports of government departments do not find them to be 'decision-useful' invites further investigation of the reporting framework that serves as the basis for compiling general purpose financial reports. Second, this research has gone some way to address the calls for further empirical research in the context of particular entities (Rutherford, 1992). This research has identified that the assumptions about the users of government department general purpose financial reports and their information needs is incomplete and misspecified. Further empirical research within the context of specific entity types within the public sector is clearly of value and could add to understanding the elements of the 'decision-useful' model for general purpose financial reporting in other entity types such as local government authorities.

TABLE I

Responses from recipients of government department annual reports by user category

Classification	Number of Responses
External users	189 (65.4%)
Ratepayer/taxpayer	25 (8.7%)
Other resource provider	38 (13.1%)
Oversight bodies	60 (20.8%)
Other like entities	59 (20.4%)
Other recipients of services	7 (2.4%)
Internal users	100 (34.6%)
Internal management	86 (29.8%)
Elected officials	14 (4.8%)
Total	289 (100%)

TABLE II

Identification of factors and the variables that comprise them

Factor	Variables
General Purpose Financial Reports	Balance Sheet Cash Flow Statement Notes to Financial Statements Operating Statement Auditor's Report
Performance Information	Summary Facts Figures & Key Statistics Financial Overview & Analysis Performance Indicators Budget versus Actual Information
Narrative Information	Overview of Entities Operations Description before Financial Statements CEO's Report

TABLE III**Mean factor scores for the emphasis placed on information**

	General Purpose Financial Reports	Performance Information	Narrative Information
All Users	3.57	3.82	3.59
External Users	3.62	3.85	3.60
Internal Users	3.45	3.77	3.57

TABLE IV**Identification of factors and the variables that comprise them**

Financial Accountability	Public Accountability	Decision Making
<ul style="list-style-type: none"> • To determine financial viability • To determine if organization can meet its short term liabilities • To determine if organization can meet its long term liabilities • To determine if organisation has adhered to budget • To determine if organization has met its objectives • To compare results with other similar organization 	<ul style="list-style-type: none"> • To determine if organization has operated in best interest of community • To determine if organisation has conducted its operations effectively • To determine if organization has conducted its operations efficiently • To decide if resources used as intended • To determine effect of current operations on future generations • To determine if public money used appropriately • To determine the effect of current operations on future funding • To make representations for funding 	<ul style="list-style-type: none"> • To decide to make representations re provision of specific programs • To decide how to vote • To determine likelihood of increased service charges • To inform a decision as a supplier of goods, services or finance • To commence use of services • To decide on continued use of organization services • To determine likelihood of increased taxes or charges • To decide whether to make representations to alter mix of services • To decide whether or not to support organization decisions

TABLE V**Mean factor scores for the use made of financial statement information**

Entity Type	Financial Accountability	Public Accountability	Decision-making
All Users	3.49	3.54	2.85
External Users	3.47	3.50	2.81
Internal Users	3.54	3.63	2.92

APPENDIX A

Legislative and regulatory adoption of accounting standards in the public sector

Jurisdiction	Legislation
Federal	Financial Management and Accountability Act 1997 Financial Management and Accountability Regulations 1997 Commonwealth Authorities and Companies Act 1997 Finance Minister's Orders
Queensland	Financial Administration and Audit Act 1977 Financial Management Standard 1997 Government Owned Corporations Act 1993 Local Government Act 1993 Local Government Finance Standard 1994
New South Wales	Public Finance and Audit Act 1983 Treasurer's Directions State Owned Corporations Act 1989 Local Government Act 1993
Victoria	Financial management Act 1994 Directions of Minister for Finance Local Government Act 1989 Local Government (Consequential Provisions) Act 1989
South Australia	Public Sector Management Act 1995 Public Finance and Audit Act 1987 Treasurer's Instructions Public Corporations Act 1993 Local Government Act 1999 Local Government (Financial Management) Regulation 1999
Northern Territory	Local Government Act (1973) Local Government (Accounting) Regulations (1973)
Tasmania	Financial Management and Audit Act 1990 Treasurer's Instructions Local Government Act 1993
Western Australia	Financial and Administration Act 1985 Local Government Act 1995

APPENDIX B

Queensland Government Departments

	Budget Allocation 1998/99 \$
Central Agencies	
Department of Premier & Cabinet	176.3m
Department of State Development	147.9m
Department of Treasury	1,371.3m
Line Departments	
Department of Health	3,701.0m
Education Queensland	3,642.9m
Department of Main Roads	1,400.4m
Queensland Transport	1,227.3m
Department of Employment, Training & Industrial Relations	818.5m
Queensland Police	752.4m
Department of Families, Youth & Community Care	591.8m
Department of Housing	540.4m
Department of Communication & Information, Local Government & Planning	524.0m
Department of Natural Resources	477.2m
Department of Corrective Services	431.6m
Department of Public Works	428.8m
Department of Justice & Attorney-General	417.8m
Department of Primary Industries	294.1m
Department of Emergency Services	170.4m
Department of Mines & Energy	166.5m
Department of Tourism Racing & Sport	166.2m
Department of Aboriginal & Torres Strait Islander Policy & Development	119.5m
Department of Equity & Fair Trading	50.9m

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¹ AAS 27 *Financial Reporting by Local Governments* (1991), AAS 29 *Financial Reporting by Government Departments* (1993) and AAS 31 *Financial Reporting by Governments* (1994).

² A general purpose financial report includes a balance sheet, income statement and cash flow statement and notes to the accounts

³ That is from other government departments.

⁴ Queensland is one of the 8 jurisdictions in the federation of Australia. It was chosen as the focus of this study initially because of accessibility of data to the researchers. However as all jurisdictions have enacted similar legislation and regulations with regard to the production of annual reports by public sector entities and the inclusion of general purpose financial reports in them (see Appendix A) there is no reason to suspect any cross-jurisdictional differences.

⁵ It only sends the financial reporting section of the reports to those people or organisations who specifically request it. As this was different to all other departments at the time, and because this introduces a self-selection bias, it was determined that it was not appropriate to include the Department of Education in the study.

⁶ It is to be noted that Statement of Accounting Concept 2 *Objective of General Purpose Financial Reporting* (SAC 2) identifies elected officials as dependent users, however, in this study, consistent with prior research (Collins et al., 1991; Taylor and Rosair, 2000 and Cheng, 1994) ‘elected officials’ are regarded as a category of ‘non-dependent’ users.

⁷ The complete set of decisions and accountabilities can be found in Table IV.

⁸ In the Coy (1997) study the response rate reflects the fact that the research instrument was sent to people who had already indicated their willingness to participate in the research by supplying their contact details to the researchers.

⁹ Question 6 of the survey instrument asked: “When reading the annual report of (name of the entity) how much emphasis do you place on: the overview of the department’s operations; the descriptive section of the annual report before the financial statements; the operating statement; the balance sheet; the cash flow statement; the notes to the financial statements; the auditors’ report; performance indicators; the chief executive officer’s report; summary facts, figures and key statistics; financial overview and analysis; disclosure of actual versus budget and variance information; remuneration of executive officers.”

¹⁰ ‘Remuneration of executive officers’ was omitted from the factor analysis as it was deemed to be a subset of the ‘notes to the financial statements’ item and consequently was at a level of specificity that differed from the remaining items.

¹¹ The factor score was obtained by summing the score on each variable contained in a factor and obtaining an average. This allowed for the differences in the number of variables that comprised each factor.

¹² A comparison at individual user category level was not possible because of small numbers in some of the user categories in some of the entity types.

¹³ A score of 2-3 was regarded as little emphasis, a score of 3-4 was regarded as some emphasis and a score of 4-5 was regarded as strong emphasis.

¹⁴ The current regulatory framework does not prevent the disclosure of performance information. AAS 29 *Financial Reporting by Government Departments* encourages the publication of

performance indicators but provides no guidance as to what types of performance measures might be appropriate or how they would be reported.